



The Arrow

BANKRUPTCY REFORM ACT SIGNED INTO LAW

President Clinton signed the Bankruptcy Reform Act of 1994 into law on October 22, 1994. There are many changes in the Bankruptcy Code contained in the new law, some of which are merely administrative, but others which have a direct impact on creditors. We will endeavor in this article to point out some changes which we believe will be of particular interest to our readership.

NON-INSIDER TRANSFEREES GIVEN PROTECTION

Back in the October, 1989 issue of *The Arrow*, in "Insiders Guaranties-A Two Edged Sword?" we reported upon the impact of the now infamous Deprizio decision, which depended upon a literal reading of the Bankruptcy Code to extend the period in which a Trustee was able to avoid a preferential transfer from ninety (90) days to one (1) year prior to the filing of the bankruptcy petition for creditors who were not insiders with respect to the Debtor when those non-insider creditors held guaranties from insiders.

Under Deprizio, a creditor who held a guaranty from any "insider" of a debtor could have a payment from the debtor to it 364 days prior to the bankruptcy petition set aside if it otherwise fit the definition of a preference. This caused many responsible creditors to discontinue the use of guaranties, although your editor thought such extreme measures an over-reaction to Deprizio.

Under the Bankruptcy Reform Act, 11 U.S.C. §546 has now been amended to include language that precludes the Trustee from recovering from a transferee that is not an insider of any otherwise avoidable transfer made between ninety (90) days and one year before the filing of the petition. The amendment reflects the dissatisfaction of many creditors with the Deprizio decision and in effect legislatively overrules it.

PERFECTION OF PURCHASE MONEY SECURITY INTERESTS

The new Act also amends 11 U.S.C. §547 to extend the Bankruptcy Code's recognition of automatic perfection of a purchase money security interest without filing from a period of ten (10) days to twenty (20) days. The purpose of this amendment is to bring the Code in line with state Uniform Commercial Code provisions with which it was previously in conflict. A creditor in a state recognizing an automatic perfection period of twenty (20) days was otherwise left in limbo if his Debtor filed a Petition fifteen (15) days after attachment of the security interest, but before filing of the financing statement.

RECLAMATION RIGHTS EXTENDED

Good news for unsecured creditors who ship on open account comes with the amendment of 11 U.S.C. §546 to provide that a seller may reclaim goods shipped to the insolvent buyer within ten (10) days

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of the receipt by the buyer as before, but also allowing the written reclamation to be made within twenty (20) days after receipt of such goods by the buyer if the usual ten (10) day period expires after the commencement of the buyer's bankruptcy case. The seller's right to reclaim goods from an insolvent buyer outside bankruptcy is still governed under Article 2-702 of the Uniform Commercial Code.

DEADLINE FOR ASSUMPTION OR REJECTION OF LEASES

Previously, if a creditor was a lessor under a "true lease" of personal property, such as rental equipment, it was incumbent upon the creditor's counsel to move to have the court set a deadline by which a Trustee or Debtor in Possession had to assume or reject the lease.

Now §365 (d) of the Code has been amended to insert an automatic sixty (60) day deadline for the Trustee or Debtor in Possession's assumption or rejection of a personal property lease (unless the property is leased to an individual primarily for personal, family or household purposes), unless the Court, after notice and a hearing and "based on the equities of the case" orders otherwise. Thus, the burden of taking action has shifted from the creditor/lessor to the Trustee or the Debtor in Possession.

RETURN OF GOODS

§546 of the Code has been amended to allow a Trustee or Debtor in possession to file a motion within 120 days after the date of the Order of Relief to return goods shipped to the Debtor by a creditor before the commencement of the case and offset the purchase price of the goods against the pre-petition claim of the creditor. The amendment requires that the return must be found, after notice and a hearing in open Court, to be in the best interest of the estate, and the creditor's consent to return of the goods and set off of the claim must be obtained. This appears to be one of those rare common sense amendments since the goods shipped are probably of more value to the shipping creditor than to the estate in most cases.

REAFFIRMATIONS

§524 (c) of the Code has been amended to include additional requirements in the wording of a Reaffirmation Agreement in order for it to be binding. In addition to the language previously required, a clear and conspicuous statement advising the debtor that the Reaffirmation Agreement is not required under the Bankruptcy Code, non-bankruptcy law, or under any agreement not in accordance with the provisions of the statute, and also adds a requirement that the attorney's Affidavit or Declaration include language to the effect that the debtor's counsel fully advised the debtor of the legal effect and consequences of the Reaffirmation and the consequences of any default by the debtor under the terms of the Reaffirmation Agreement.

As a practical matter, this means that all reaffirmation forms used by creditors must now be reworded for use in bankruptcies filed after October 21, 1994.

CREDITOR COMMITTEE EXPENSES

11 U.S.C. §503 (b)(3) has been amended to make clear now that a member of an Official Creditors' Committee is entitled to reimbursement of his or her expenses if such expenses "are incurred in the performance of the duties of such committee." The courts have previously allowed reimbursement of the expenses of members of creditors' committees, but had to stretch the Code a bit to arrive at that result.

SECURITY INTEREST IN POST PETITION RENTS PROTECTED

§552(b) has now been amended to protect those creditors holding a security interest in post-petition rents and lodging payments. The amendment provides that if there was a pre-petition security agreement which extended to after acquired property and to amounts paid as rents of such property, or the fees, charges of accounts, or other such payments for the use or occupancy of rooms and other public facilities in hotels, motels or other such lodging properties, then the security interest is extended to post-petition rents, fees, charges of accounts or other such payments after the commencement of the case. Of course, the security interest in question has to have been properly recorded.

This amendment brings quite a change to Chapter 11 filings involving motel and hotel properties. Previously, some courts have held that post-petition rent and room payments – in essence, the income stream of such debtors – were not necessarily subject to a creditor's security interest unless the creditor had already foreclosed upon the property and had a receiver appointed. Mortgage holders will now clearly be able to lay claim to the debtor's income stream as cash collateral during the course of a Chapter 11.

LUXURY GOODS EXCEPTION TO DISCHARGE

§503 (a)(2) has been amended to extend the present forty (40) day period prior to a petition in which the debtor's purchase of "luxury goods or services" are presumed non-dischargeable to sixty (60) days, but the amount of such purchases has been increased from \$500 to \$1,000 before the presumption comes into play. The new law also increases from twenty (20) to sixty (60) days prior to the petition date the period in which cash advances aggregating more than \$1,000 are presumed to be non-dischargeable.